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479352—42

In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 282

GEORGE W. MASON AND HAZEL B. MASON, HIS WIFE, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 15–22) is reported at 41 B. T. A. 1287. The opinion of the Circuit Court of Appeals (R. 58–61) is reported at 125 F. (2d) 540.

JURISDICTION

The judgment of the Circuit Court of Appeals for the Sixth Circuit was entered on January 14, 1942 (R. 57), and its order denying the petitioners' petition for rehearing (R. 63–75) was entered on

March 6, 1942 (R. 77). Two orders extending the time to file the petition for a writ of certiorari having been granted by this Court (R. 78), the petition was filed on August 5, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The taxpayer [1] entered into a contract of employment with the Kelvinator Corporation providing, together with other compensation, a bonus, measured in money, computed on the net earnings of the employer, but with a further provision obligating the taxpayer to exchange the bonus money, immediately upon receipt, for stock of the employing company at a fixed value. The market value of the stock thus received by the taxpayer in 1935 was considerably in excess of the "bonus money."

The question presented is whether the taxpayer realized taxable income in the amount of the "bonus money" or in the amount of the fair market value of the stock.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in

[1] The word "taxpayer," wherever used herein, refers to petitioner, George W. Mason.

> whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

> ART. 22 (a)–3. Compensation paid other *than in cash*.—If services are paid for with something other than money, the fair market value of the thing taken in payment is the amount to be included as income. If the services were rendered at a stipulated price, in the absence of evidence to the contrary such price will be presumed to be the fair value of the compensation received. If a corporation transfers to its employees its own stock as compensation for services rendered by the employee, the amount of such compensation to be included in the gross income of the employee is the fair market value of the stock at the time of the transfer. * * *

STATEMENT

The facts as stipulated (R. 9–15), and as found by the Board of Tax Appeals (R. 16–20), are substantially as follows:

The taxpayer and his wife filed a joint return for the taxable year 1935. On September 7, 1933, the

taxpayer entered into a four-year contract with the Kelvinator Corporation (hereafter called the corporation), effective October 1, 1933, superseding and terminating as of the latter date a previous contract of employment dated March 14, 1931, which would otherwise have expired on December 10, 1934. The new contract of employment [2] provided, in substance, that the taxpayer's regular, fixed rate of compensation should be (1) $50,000 annually; (2) 1,250 shares of the corporation's fully paid stock, and (R. 11–12):

> (3) The corporation further agrees as further compensation to Mason to pay him on January 15, 1935, 1936, 1937 and 1938, a sum equal to ten per cent (10%) of the net earnings of the preceding fiscal year, determined as hereinafter set forth after deducting therefrom an amount equal to five per cent (5%) upon the capital and surplus of the corporation determined as hereinafter set forth. The corporation agrees to sell and Mason agrees to purchase at ten dollars ($10.00) per share on January 15th of each year as above set forth a number of shares of fully paid stock of the corporation equal to the sum, if any, payable to Mason on such date pursuant to the preceding section of this paragraph (3); provided, that hereunder the corporation will not pay in

[2] Only the material portions of the contract are summarized here. The provisions of the contract in its entirety are set forth in the stipulation of facts (R. 10–15), and in the Board's opinion (R. 16–20).

> excess of $400,000 nor may Mason purchase in excess of 40,000 shares of such stock during the term of the contract; and provided further that the corporation will not pay in excess of $100,000 nor may Mason purchase in excess of 10,000 shares of such stock in any one year except that (a) for any year of this contract the corporation may and will pay Mason such an amount as will make the total payment to Mason under this paragraph (3) $100,000 per annum for each year of this contract theretofore expired in case 10% of the net earnings since October 1, 1933, computed under the formula therein set forth shall equal or exceed $100,000 per annum for the years already expired and (b) Mason may and will purchase such number of shares as will make the total number of shares purchased by him under this paragraph at $10.00 per share equal the amount paid him under the above exception (a).

The amount determined as payable to the taxpayer on January 15, 1935, computed upon net earnings of the corporation for the preceding year under Paragraph (3) of the contract, was $49,891.60. Pursuant to the provisions of that Paragraph, he acquired 4,989 shares of the capital stock of Kelvinator Corporation on that date, having a then fair market value of $84,189.38. On September 7, 1933, when the above contract was executed, the stock in question had a fair market value of $11.4375 per share. The taxpayer devoted his entire time to the affairs of Kelvinator Cor-

poration during the taxable year. (R. 20.)

In making their return for the calendar year 1935, the taxpayer and his wife included in income the amount of $49,891.69. In determining the deficiency the Commissioner increased the reported income by the difference between this amount and $84,189.38, the fair market value of the stock acquired. (R. 20.)

On the basis of these facts, the Board held that the taxpayer realized taxable income in the amount of the fair market value of the stock when received in the taxable year 1935 (R. 22). The court below affirmed (R. 58–61).

ARGUMENT

The issue in this case is whether the stock in question was received by petitioner as compensation for services. Under the contract the company agreed to pay him as a bonus on January 15 of each year 10% of its net earnings, and he agreed to purchase on the same day, at $10 a share, the number of shares of stock "equal to the sum" payableto him. The record does not disclose whether the company and petitioner actually went through the ritual of handing the price of the shares back and forth. Whether they did or not, the net result, as intended by the parties, was that at the close of the day petitioner had received as compensation for services, and there-

fore as income, stock worth more than $10 per share. The measure of such compensation, under the statute and regulations (see pp. 2–3, *supra*), is the fair market value of the stock at the time of transfer. The decision below is thus plainly correct, and is in accord with established principles. ~~*Cf. Olson* v. *Commissioner*, 67 F. (2d) 726 (C. C.~~ Cf. *Olson* v. *Commissioner*, 67 F. (2d) 726 (C. C. A. 7), certiorari denied, 292 U. S. 637; *Robinson* v. *Commissioner*, 59 F. (2d) 1008 (C. C. A. 6); *Rodrigues* v. *Edwards*, 40 F. (2d) 408 (C. C. A. 2).

Petitioner contends that the decision below conflicts with *Omaha National Bank* v. *Commissioner*, 75 F. (2d) 434 (C. C. A. 8). There is language in that opinion which seems unduly to sanctify the formal terms of the contract. But the purchase of stock in that case was separable from the credit or bonus granted the taxpayer by his employer. The taxpayer could pay for the stock independently of such credits; he was entitled to delivery "whenever he paid the difference between the credits and the purchase price" (p. 434). This provision may have been sufficient to justify characterizing the entire contract as one of purchase and sale, even in so far as the stock acquired through company credits was concerned. Accordingly the court below here held the *Omaha National Bank* case to be distinguishable (R. 60).

CONCLUSION

The decision of the court below is in accord with established principles. There is no conflict and the petition should be denied.

Respectfully submitted.

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